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Volume 6, Issue 10

October 2025

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How to Operate a Captive Like a Real Insurance Company (and Stay Compliant)



By Joseph W Tucciarone, CEO National Network of Accountants

Captive insurance is one of the most powerful tools for businesses seeking control of risk, cost savings, and long-term financial strength. But forming a captive is just the first step. To remain compliant and achieve real benefits, a captive must be run like a legitimate insurance company—not simply a tax strategy on paper.

Below are the essential practices that separate credible captives from those that face regulatory or IRS challenges.

1. Issue Policies on Time

Commercial insurers issue clear, written policies each year. Captives must mirror this professionalism. Policies should:

- Be drafted or reviewed by qualified insurance professionals.
- Reflect genuine, commercially reasonable risks.
- Be delivered to insured entities on schedule.

Failure to issue policies—or delivering them long after premiums are paid—is a major red flag for regulators and auditors.

2. Set and Collect Actuarially Sound Premiums

Premiums cannot be arbitrary. They must be supported by actuarial analysis of risk, claims history, and industry benchmarks. Best practices include:

- Using independent actuaries annually.
- Documenting assumptions and methodology.
- Collecting premiums on a fixed, timely schedule.

Late or inconsistent payments may suggest the captive is a tax shelter rather than a real insurer.

3. Manage Claims Professionally

A captive must demonstrate it can pay claims fairly. That means:

- Having a formal claims procedure.
- Using administrators or third-party adjusters when needed.
- Documenting every step from submission to resolution.

Even if claims are rare, a structured process proves operational credibility.

4. Maintain Adequate Capital and Reserves

Captives must comply with domicile capitalization requirements and hold reserves to cover claims.

Owners should:

- Monitor reserves regularly.
- Reinvest underwriting profits into the captive.
- Avoid early withdrawals, especially in initial years.

Strong capitalization reassures regulators and proves financial stability.

5. Document Everything

Documentation is your compliance shield. Keep detailed records of:

- Board meetings and governance.
- Policy issuance and renewals.
- Premium invoices and payments.
- Claims handling.
- Actuarial reports and financials.

Thorough documentation is critical if your captive is ever questioned.

6. Work With Qualified Service Providers

Captives thrive through professional support, including:

- Licensed captive managers.
- Actuaries, underwriters, and accountants.
- Legal counsel with tax and insurance expertise.

These experts ensure your captive meets both regulatory and tax standards.

7. Stay Current with Regulatory Changes

The captive industry evolves constantly. To remain compliant:

- Track updates from your domicile.
- Engage in industry associations.
- Conduct periodic compliance reviews with advisors.

The Payoff: Credibility and Control

When run properly, a captive delivers:

- Financial strength through retained profits.
- Flexibility to design custom coverage.
- Stability against rising commercial premiums.
- Credibility with regulators, auditors, and lenders.

Cutting corners—such as late premiums, missing policies, or poor claims processes—can quickly undermine your investment.

Final Thought

Owning a captive is both a privilege and a responsibility. Treat it like a true insurance company from day one—issuing policies on time, charging actuarially sound premiums, handling claims properly, and documenting everything. Doing so keeps you compliant and maximizes the long-term value of your investment.

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